

Third, BellSouth's efforts to screen local competition from the public interest analysis conflict with the legislative history of the Act. Making selective use of this history (see Br. 68), BellSouth omits mention of the most directly pertinent point: During deliberations over the Act, the Senate tabled -- by a vote of 68 to 31 -- an amendment providing that "[f]ull implementation of the [competitive] checklist . . . shall be deemed in full satisfaction of the public interest, convenience, and necessity." 141 Cong. Rec. S7960, S7971 (daily ed. June 8, 1995).<sup>46</sup> Congress's deliberate decision to keep the "public interest" test as a separate and independent requirement establishes that satisfaction of the checklist is no substitute for actual effective local competition that would justify BOC long distance entry.<sup>47</sup>

**C. Because The Interexchange Market Is Already Vigorously Competitive, BellSouth's Claims Of Likely Consumer Benefits From Its Entry Are Baseless.**

In arguing that its entry would be in the public interest, BellSouth predicts that its entry into the interexchange market would produce tremendous benefits by making that market more competitive. In particular, it cites "welfare analyses" of the WEFA Group and Professor Jerry

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<sup>46</sup> The Conference committee adopted this provision from the Senate Bill. See Conf. Rep. p. 149.

<sup>47</sup> In addition, Congress expressly concluded that the MFJ's section VIII(C) test -- "whether there is no substantial possibility that the BOC or its affiliates could use monopoly power to impede competition in the market such company seeks to enter" -- would be an appropriate standard for the Attorney General, and thus the Commission, to employ in evaluating a BOC's application. See Conf. Rep., p. 149. The MFJ court consistently construed the VIII(C) standard to require an examination of the competitive conditions in the BOC's local market in order to assess whether the BOC continued to enjoy a bottleneck monopoly power that could be leveraged into market power in the market the BOC sought to enter. See, e.g., United States v. Western Elec. Co., 673 F. Supp. 525 (D.D.C. 1987), aff'd on this ground, 900 F.2d 283 (D.C. Cir. 1990), cert. denied, MCI Communications Corp. v. United States, 498 U.S. 911 (1990).

Hausman, who each contend that BellSouth's in-region, interLATA entry will drive down long distance prices and stimulate the economy. But the logic of these witnesses is untenable: They anticipate enormous benefits from the entry of one firm into a market that already has hundreds of firms openly fighting for customers, but perceive (to the extent they address the issue at all) only "very small" gains from the removal of entry barriers in a local market that has long been dominated by a single monopolist. Hausman Aff. ¶ 25. To put BellSouth's claims into perspective, a modest \$0.01 per minute reduction in the price of local calls could save consumers on the order of \$15 billion per year, more than twice the annual savings estimated by BellSouth (Br. i) from reducing long distance prices an extraordinary 18 percent. Hubbard/Lehr Aff. ¶ 112 & n.80.

BellSouth's extravagant claims of public benefit depend on mischaracterizations of both local exchange and interexchange markets. As discussed above, permitting BellSouth to enter the interexchange market while it retains monopoly control of the local exchange market will harm competition in both the local and long distance markets. Moreover, because the long distance market already displays the hallmarks of a vigorously competitive market -- hundreds of new entrants; declining market share of the formerly dominant carrier; excess capacity; a high rate of customer churn; and declining prices -- BellSouth's premature entry into that market will not bring the consumer benefits BellSouth promises.

The long distance market is characterized by intense rivalry among several hundred aggressive competitors. Hubbard/Lehr Aff. ¶¶ 20-45. Moreover, since divestiture, AT&T has steadily lost long distance market share. In South Carolina, its share of residential long distance revenue is less than 53%. Federal Communications Commission, Long Distance Market Shares,

Industry Analysis Division, Common Carrier Bureau, July 1997, p. 21, Table 10. Nationwide, AT&T's share of toll revenue has dropped from 88% in the first quarter of 1984 to 51% by the first quarter of 1997 -- an average decline of nearly 3% per year. Id. at 18, Table 8. Furthermore, AT&T's losses were not just MCI and Sprint's gains. More than three quarters of AT&T's losses between the first quarter of 1990 and the first quarter of 1997 were to hundreds of smaller interexchange carriers: As AT&T's share of revenues fell by 17.4% during this period, MCI's share increased by only 3.3% and Sprint's share increased by only 0.1%. Id. At the same time, WorldCom's share of revenues grew from 0.2% to 6.8%, and the share of the remaining carriers grew from 8.3% to 15.8%. Id. It is simply preposterous to suggest that these hundreds of firms, widely differentiated by size and geographic scope, could tacitly collude or engage in oligopolistic forbearance.

The competitive significance of the hundreds of interexchange firms is heightened by the long distance market's widespread excess capacity. Excess capacity fosters competitive pricing, because where competitors can readily expand output to meet customer demand, the market power of a firm contemplating an anticompetitive price increase is muted. See United States Department of Justice, Horizontal Merger Guidelines § 2.22 (1992). There is so much spare fiber optic capacity in the interexchange industry that AT&T's competitors could absorb one-third of AT&T's capacity within three months simply by using spare switch ports and existing transport facilities. Motion of AT&T to be Reclassified as a Non-Dominant Carrier, 11 FCC Rcd. 3271, 3303-3304 (1995) ("Non-Dominance Order"). As the FCC has concluded, "AT&T's competitors have enough readily available excess capacity to constrain AT&T's pricing behavior

-- i.e., that they have or could quickly acquire the capacity to take away enough business from AT&T to make unilateral price increases by AT&T unprofitable." Id. at 3303.

The intensity of competition in the long distance market is also evidenced by the frequency with which customers switch carriers. For example, in 1995, over 42 million long distance subscribers changed carriers. In 1996, after a steady barrage of price-based advertising and promotion, this number rose to 53 million subscribers. Hubbard/Lehr Aff. ¶ 44. This pronounced willingness and ability of consumers to switch long distance carriers is patently incompatible with the specious claim that the long distance market is not subject to effective competition.

Finally, the declining price of interexchange service since divestiture is perhaps the most stark evidence of competition. Since the MFJ, long distance prices have plummeted 60% in real terms, and 37% net of access. Hubbard/Lehr Aff. ¶ 31. The decline in prices has not been limited to the highest volume callers. To the contrary, as the FCC has found, the "average best price" for all categories of residential customers divided by calling volume fell from 1991 to 1995. Non-Dominance Order, 11 FCC Rcd. at 3363 (Appendix B, Table 1).<sup>48</sup>

Thus, after an objective examination of the relevant determinants of market power, there can be no tenable claim that the long distance market is non-competitive. In contending otherwise, BellSouth and its experts rely principally on assertions that AT&T's rates have risen notwithstanding significant reductions in access charges. BellSouth Br. 73-74; Hausman Aff. ¶¶ 28-32; Schmalensee Aff. ¶ 9. Those claims are false. They directly conflict with the

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<sup>48</sup> The FCC's data showed a slight increase in nominal terms for the customers in the lowest calling volume category, but even that segment experienced a decline in real terms.

Commission's findings, and they ignore data that conclusively show that rates paid by consumers have declined more than access charge reductions precisely because of the intense competition in that market. Hubbard/Lehr. Aff. ¶¶ 31-32; 119-122.

Discounting the benefit to low-volume customers occasioned by recent reductions in IXC's basic rates, BellSouth also relies on the fact that basic schedule rates for low-volume customers have increased in recent years. But under the many flat rate plans offered by major IXCs, even low-volume customers need not pay basic rates. BellSouth's contention that many consumers cannot benefit from these plans is false. BellSouth Br. 74. For example, customers who make most of their calls during peak times can benefit from AT&T's flat \$0.15 rate, while customers who make most of their calls on evenings and weekends can benefit from Sprint's \$0.10 off-peak rate. These flat rate plans also plainly refute BellSouth's specious contention that even "mid-volume callers are denied discounts." BellSouth Br. 75.

Moreover, increases in basic rates have occurred for competitively benign reasons. Because regulation has kept rates below cost for low-volume customers, AT&T has raised those rates when permitted to do so, and its competitors have followed suit, presumably to avoid attracting low-volume, high cost customers themselves.<sup>49</sup> The measure of competition is not at the low end of the market, where regulation has artificially depressed prices, but at the middle and high-volume end, where rates can reflect costs and carriers compete aggressively on price and quality to win customers. BellSouth never even attempts to explain why, if long distance carriers can successfully collude, they have offered discounts to high volume customers who

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<sup>49</sup> See B. Douglas Bernheim and Robert D. Willig, The Scope of Competition in Telecommunications (AEI 1997) (unpublished manuscript), Chapter 2, pp. 37-43.

provide the most revenue -- or why, if these carriers can collude on price, they do not collude on non-price matters and instead choose to "waste" enormous sums on advertising and other marketing expenditures.

Nor does BellSouth adequately explain (Br. 80) why its "marketing strength will be most pronounced" among low-volume customers, and it offers no plausible reason why it would choose to target the least profitable section of the long distance market.<sup>50</sup> In the absence of such evidence, there is no reason to believe that BellSouth's entry will bring any of the benefits of competition to low-volume long distance customers. See Ameritech Michigan Order ¶ 16 ("[I]n determining the extent to which BOC entry into the long distance market would further competition, we would find it more persuasive if parties presented specific information as to how such entry will bring the benefits of competition, including lower prices, to all segments of the long distance market.").

Also unfounded is BellSouth's argument that SNET's entry into the long distance market illustrates the positive competitive impact of BOC entry into interchange markets. To the contrary, SNET's long distance prices are no lower than major IXCs' nationwide rates. SNET's interexchange rates vary from 23 cents during the day to 13 cents at night (or a 15 cent flat rate), and only provide small discounts for high volumes. In comparison, AT&T One Rate and Sprint Sense Day Plan each offer flat rates of 15 cents per minute to all customers, at all times, regardless of calling volumes. In addition, for a \$4.95 monthly fee, AT&T offers a 10 cent flat

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<sup>50</sup> It is far more likely that BellSouth will follow GTE's reported "targeted approach of wooing high volume customers." Communications Daily, 12/3/96, p.1 The article goes on to quote GTE's "President - long distance services" Rob McCoy as explaining, "We're not going after the mass market. That would be inefficient." Id.

rate at all times. Sprint also offers a flat rate of 10 cents per minute for domestic calls between 7 P.M. and 7 A.M., and 25 cents per minute for other domestic calls, and it has recently introduced a plan that offers \$50.00 per month of free calls on Monday evenings. MCI offers a flat rate of 12 cents at all times to customers who make over \$15.00 a month in calls, and it offers all residential customer a 5 cent per minute rate on Sundays. Hubbard/Lehr Aff. ¶ 109. Plainly, even taking into account SNET's one-second billing increments, these statistics reveal no obvious consumer benefits flowing from SNET's entry into the interexchange market.

Nor is the fact that SNET has captured significant market share attributable to SNET's greater efficiency. SNET's success is due in large part to its bundling of long distance offerings with its monopoly provision of local services and its aggressive promotion of PIC freezes for its own long distance customers. Hubbard/Lehr Aff. ¶ 110. Moreover, SNET has recently announced that it will undertake a corporate reorganization expressly designed to rid itself of the Act's requirement that it resell local services at a wholesale discount.<sup>51</sup> Thus, far from proving the benefits of permitting a monopoly ILEC into an in-region, interLATA market, SNET's behavior in Connecticut illustrates what an ILEC unconstrained by the section 271 incentive will do to avoid opening its local market to competition.

BellSouth's reliance on the Bell Atlantic/NYNEX Eastern corridor interLATA rates is also misplaced. Although a customer can now presubscribe to Bell Atlantic/NYNEX for Eastern corridor calls, the customer must then dial a 10-XXX carrier access code for all interLATA calls that are not Eastern corridor. As a result, very few customers have presubscribed to Bell

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<sup>51</sup> See AT&T v. Commissioners of the Connecticut Dep't of Pub. Util. Control, Civ. Action No. 397CV01601, Complaint for Injunctive Relief and Declaratory Judgment, ¶ 9 (filed Aug. 8, 1997).

Atlantic/NYNEX in the corridor, and almost all Eastern corridor BOC calls require a carrier access code. It is these obvious competitive handicaps, and not greater efficiencies, that have forced Bell Atlantic/NYNEX to offer lower prices. Hubbard/Lehr Aff. ¶ 110 n.78.

BellSouth's claim that it will spur competition by underpricing long-distance carriers is thus implausible in the extreme, for prices are already at competitive levels, and BellSouth can achieve no cost advantages except through discrimination, cross-subsidies, and price squeezes. For this reason, BellSouth's reliance upon the WEFA Group's estimate of the impact of BellSouth's in-region interLATA entry on the South Carolina economy is wholly specious. WEFA's conclusions are based on assumptions -- such as that BellSouth's entry will reduce long distance service prices by 25% -- that are empirically unjustified and patently unreasonable. Hubbard/Lehr Aff. ¶¶ 124-126. Moreover, the WEFA study's welfare benefit analysis is also rendered meaningless by its failure even to address the harm to local and long distance consumers -- whose savings from the advent of meaningful local competition would dwarf any savings that might flow from adding yet another long distance competitor (see Hubbard/Lehr Aff. ¶ 112) -- that would be caused by permitting BellSouth to enter the in-region interLATA market before entry barriers to the local market are removed.

BellSouth's present claim that it will offer "initial basic rates" that are "at least 5% lower than the corresponding rates of the largest interexchange carrier" (Br. 78) illustrates the illusory nature of BellSouth's promises: In light of the numerous discount plans available to long distance customers, it is simply absurd to base a claim of lower long distance prices solely upon a proposed "initial" discount off basic rates that no consumer need pay.



There is in any event no reason to think that BellSouth's promises of future price-cuts will be kept any more faithfully than the promises several BOCs made to persuade the MFJ court to permit them to offer long distance service to cellular customers. While Ameritech, SBC, and others projected that they would charge cellular customers about 10 cents a minute,<sup>52</sup> in practice their flat rates are about twice that much.

It is thus far more likely that BellSouth's entry will comport with the expectations of Pacific Telesis. Internal and proprietary documents of Pacific Telesis candidly acknowledge that "[l]ong distance is one of the most competitive businesses in America," and that Pacific Telesis' own costs in long distance would be significantly higher than AT&T's.<sup>53</sup> As a result, Pacific Telesis' own witness has admitted that Pacific Telesis does not appear "headed for the Price Club segment of the market" and will instead be at the "Nordstrom's end of the market."<sup>54</sup>

### CONCLUSION

For the foregoing reasons, BellSouth's section 271 application for South Carolina should be denied.

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<sup>52</sup> United States v. Western Elec. Co., No. 82-0192 (D.D.C.), Reply of the Bell Companies In Support of their Motion for Removal of Mobile and other Wireless Services From the Scope of the Interexchange Restriction, Affidavit of R.S. Higgins and J.C. Miller III, ¶¶ 20, 30 n.5 (Aug. 3, 1992).

<sup>53</sup> The documents remain confidential and proprietary to Pacific Telesis. These excerpts were made part of the public record in the state regulatory proceeding concerning certification of Pacific Telesis' affiliate as an interLATA carrier in California. See California Public Utilities Commission Proceeding, Application 96-03-007, Tr. Vol. 4, pp. 494, 496, 503-04.

<sup>54</sup> Id. Tr. Vol 10, p. 1272.

Respectfully submitted,

Mark C. Rosenblum /ns

Mark C. Rosenblum  
Leonard J. Cali  
Roy E. Hoffinger  
Stephen C. Garavito

Its Attorneys

Vivian V. Furman  
Karen E. Weis

AT&T Corp.  
295 North Maple Avenue  
Basking Ridge, NJ 07920  
(908) 221-3539

Kenneth P. McNeely  
AT&T Corp.  
1200 Peachtree Street, N.E.  
Promenade I, Room 4036  
Atlanta, GA 30309  
(404) 810-8829

October 20, 1997

David W. Carpenter /ns

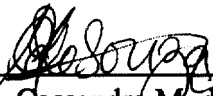
David W. Carpenter  
Mark E. Haddad  
Ronald S. Flagg  
Lawrence A. Miller  
George W. Jones, Jr.  
Richard E. Young

Sidley & Austin  
1722 Eye Street, N.W.  
Washington, D.C. 20006  
(202) 736-8000

Counsel for AT&T Corp.

## CERTIFICATE OF SERVICE

I, Cassandra M. de Souza, do hereby certify that I caused a copy of the foregoing Comments of AT&T Corp. in Opposition to BellSouth's Section 271 Application for South Carolina to be served by hand delivery, unless otherwise noted, this 20th day of October, 1997, on all parties on the attached service list.

  
\_\_\_\_\_  
Cassandra M. de Souza

## SERVICE LIST

William Caton  
Office of the Secretary  
FEDERAL COMMUNICATIONS  
COMMISSION  
Room 222  
1919 M Street, NW  
Washington, DC 20554

The Honorable Reed E. Hundt  
Chairman  
FEDERAL COMMUNICATIONS  
COMMISSION  
1919 M Street, NW, Room 814  
Washington, DC 20554

The Honorable Susan Ness  
Commissioner  
FEDERAL COMMUNICATIONS  
COMMISSION  
1919 M Street, NW, Room 832  
Washington, DC 20554

The Honorable Rachelle B. Chong  
Commissioner  
FEDERAL COMMUNICATIONS  
COMMISSION  
1919 M Street, NW, Room 844  
Washington, DC 20554

The Honorable James H. Quello  
Commissioner  
FEDERAL COMMUNICATIONS  
COMMISSION  
1919 M Street, NW, Room 802  
Washington, DC 20554

Janice Myles  
Policy and Program Planning Division  
Common Carrier Bureau  
FEDERAL COMMUNICATIONS  
COMMISSION  
Room 544  
1919 M Street, NW  
Washington, DC 20554

Michael K. Kellogg  
Austin C. Schlick  
Kevin J. Cameron  
Jonathan T. Molot  
KELLOGG, HUBER, HANSEN,  
TODD & EVANS, P.L.L.C.  
1301 K Street, NW  
Suite 1000 West  
Washington, DC 20005

\*F. David Butler, General Counsel  
SOUTH CAROLINA PUBLIC  
SERVICE COMMISSION  
111 Doctors Circle  
P.O. Box 11649  
Columbia, SC 29211

ITS, Inc.  
1231 20th Street, NW  
Washington, DC 20036

Donald J. Russell  
U.S. DEPARTMENT OF JUSTICE  
Antitrust Division, City Center Building  
1401 H Street, NW  
Suite 800  
Washington, DC 20530

\*delivery by courier

Joel Klein  
Acting Assistant U.S. Attorney  
U.S. DEPARTMENT OF JUSTICE  
950 Pennsylvania Avenue, NW  
Washington, DC 20530-001

\*delivery by courier